TCEQ DOCKET NO. 2013-1871-UCR

CONSIDERATION OF A COMMISSION ORDER SETTING THE COMPENSATION AMOUNT FOR THE DECERTIFICATION OF MONARCH UTILITIES I, L.P. FROM A PORTION OF CERTIFICATE OF CONVENIENCE AND NECESSITY NO. 12983; APPLICATION NO. 37655-C	§ § § § § § § § §	**TEXAS COMMISSION ON ENVIRONMENTAL QUALITY**

BRIEF OF MONARCH UTILITIES I, L.P.

TO THE HONORABLE COMMISSIONERS:

In response to the Texas Commission on Environmental Quality's ("TCEQ" or "Commission") letter dated October 18, 2013, Monarch Utilities I, L.P. ("Monarch") submits this brief regarding the appraisals for the compensation determination for the expedited release of a portion of Monarch's certificate of convenience and necessity ("CCN").

I. INTRODUCTION

Under Texas Water Code § 13.041, Monarch is required to provide "continuous and adequate" service to its customers. While the Legislature has provided an avenue for landowners to be released from a CCN to provide this service, the Legislature also required that the utility be fairly compensated as part of that process. A utility cannot appropriately plan to meet its statutory obligation to provide continuous and adequate service for its existing and future customers unless it can be assured that it will be fairly compensated if landowners petition to be released from the utility's service area. If landowners are permitted to cherrypick their way out of a utility's CCN without the utility being fairly compensated, it will be impossible for utilities to complete the planning and construction that is necessary to provide continuous and adequate service as required by law. Without just compensation, the utility's remaining customers are left to pay for the expenditures and planning that the utility undertook on behalf of the service area being decertified. For the reasons addressed herein, the conclusions reached in the appraisal completed by Jones-Heroy and Associates ("JHA") should be adopted to adequately compensate Monarch in this proceeding.

II. DISCUSSION

The factors set forth in 30 Tex. Admin. Code § 291.113(k) provide a means to evaluate the "just and adequate" compensation to a utility. These factors include: (1) the amount of the retail public utility's debt allocable for service to the area in question; (2) the value of the service facilities of the retail public utility located within the area in question; (3) the amount of any expenditures for planning, design, or construction of service facilities that are allocable to service to the area in question; (4) the amount of the retail public utility's contractual obligations allocable to the area in question; (5) any demonstrated impairment of service or increase of cost to consumers of the retail public utility remaining after the decertification; (6) the impact on future revenues lost from existing customers; (7) necessary and reasonable legal expenses and professional fees; and (8) other relevant factors. Using these factors, the third appraiser, B&D Environmental, Inc. ("B&D") concluded that Monarch should be compensated in the amount of $275,512. For the reasons set forth below, Monarch disagrees with the third appraiser's conclusions for Factors 1, 3, 5, and 8 and seeks $3,748,489 for the property associated with the transfer of the CCN.

Factor 1 - The amount of retail public utility's debt allocable for service in the area in question: $204,100

When analyzing the issue of debt, B&D concluded that "[e]ven if the Windy Hill Tract was never developed, Monarch's debt portion of its rate base would still be recovered through the return component of its currently approved rates by revenues generated from its current customer base and any future customers added outside the Windy Hill Tract."[1] However, Monarch has not been, and is not currently, earning a return through its rates. Therefore, Monarch's debt portion of rate base is not being recovered through return as B&D suggests.

Despite the inability to earn a return through its rates at this point in time, Monarch has invested substantially in facilities to provide continuous water service to all of its customers statewide, including those in the Plum Creek water system CCN. Monarch's existing customers share equally in the cost of the debt payments, making it reasonable to pro rate the debt service costs among all Monarch's customers. As presented in the JHA appraisal, the Net Present Value ("NPV") share of future debt service payment attributed to Windy Hill amounts to $204,100.[2]

Factor 3 - The amount of any expenditures for planning, design, or construction of service facilities that are allocable to service to the area in question: $528,989

The facilities within the Plum Creek water system contribute to providing adequate and reliable service across Monarch's service area. The planning, design, and construction of the existing facilities within the Plum Creek water system have accounted for the future service to undeveloped portions of the service area, such as the Windy Hill Tract. The July 19, 2013 JHA appraisal describes the numerous steps taken in the 2011 Plum Creek Master Plan to provide service to the area.[3] JHA's analysis concluded that the existing regional facilities constructed with the intent to share in the reliable service of the Windy Hill Tract should be included.[4] The NPV of the incremental depreciated share of the facilities that would have been recovered

---

1 B&D Appraisal at 3 (Aug. 14, 2013).

2 JHA Appraisal at 2-3 (July 19, 2013).

3 JHA appraisal at 3-5 (July 19, 2013).

4 *Id.*

through increased revenues as a result of the build out is $520,600, and the legal fees incurred by Monarch related to drafting and negotiating the development agreements totaled $8,389.[5]

However, B&D's appraisal only permits the recovery of $8,389 in legal fees and $8,223 in engineering fees that were allocable to the service area in question, for a total of $16,612.[6] For the construction portion of this factor, B&D concluded that no expenditures could be found for the construction of facilities based on Plum Creek system's lack of excess capacity to provide service to additional connections. In reaching this conclusion, B&D ignores the fact that the capacity exception received by Monarch is very common for water utilities in Texas. A capacity exception recognizes the actual use of a system and benefits the customers by the tailoring of the system to their needs. The exception allows the right amount of improvement for service within the subject system. The existence of a capacity exception does not necessarily lead to the conclusion that the system does not have excess capacity to provide service to additional connections. In fact, JHA concluded that it is appropriate to assume that the basis for the TCEQ's capacity exception will not change in the future for the existing customers of the Plum Creek system.[7]

In reality, Monarch has the necessary water supply to serve the Plum Creek system. The existing storage and pumping facilities are designed and constructed to support the type of development proposed within the Windy Hill Tract. The existing facilities provide valuable efficiencies because the additional pumps and water supplies could be integrated into the existing network to meet Windy Hill's future development demands. Monarch has shown an excess capacity available to the Windy Hill Tract at full build-out in the 2011 Master Plan.

---

[5] JHA Appraisal at 4 and Table 5 (July 19, 2013).

[6] B&D Report at 3 (Aug. 14, 2013).

[7] JHA Report at 2 (July 26, 2013).

Additionally, JHA concluded that the existing water supply wells and contract with Guadalupe-Blanco River Authority ("GBRA") would serve as a "reliable, redundant, and economical supply" for the base demands of the Windy Hill Tract.[8]

Finally, Monarch's CCN covers areas both inside and outside of the boundaries of the Barton Springs/Edwards Aquifer Conservation District ("BSEACD"). The Windy Hill Tract itself is completely surrounded by the BSEACD. However, Windy Hill claimed that Monarch would not be able to amend the transfer permit from BSEACD to include the tract and serve within its boundaries. This claim is baseless. The BSEACD has communicated to Monarch that the permit could be amended and characterized that process as a simple administrative procedure.[9]

Monarch should be permitted to recover the $528,989 in costs associated with planning, design, or construction of facilities that are allocable to the Windy Hill Tract.[10]

Factor 5 - Any demonstrated impairment of service or increase of cost to consumers of the retail public utility remaining after the decertification: $708,800

B&D calculated the amount of impairment of service or increase of cost to consumers to be $221,702. This conclusion ignores the fact that the 2011 Plum Creek Master Plan shows the Windy Hill Tract development included a 12-inch water main that was intended to serve the dual purpose of providing a looped connection and fire flows to approximately 800 existing customers in the southeast portion of the Plum Creek system. As a result of the decertification, Monarch will need to construct a 12-inch waterline for approximately 8,500 feet in a private easement. Prior to this decertification, these costs would have been shared and more efficient.

---

[8] JHA Report at 7 (July 26, 2013).

[9] August 9, 2013 Letter from Gary Rose to Lambeth Townsend..

[10] JHA Report at 3-4 (July 19, 2013).

JHA determined that 50% of the construction costs ($650,300) should be included and 100% of the costs for the private easement ($58,500) that otherwise would not have been necessary.[11] However, B&D calculated this construction cost figure based as the percentage of Windy Hill's make up of the Plum Creek System (9.60%).[12] This calculation is not appropriate because a simple comparison of the size of Windy Hill to the entirety of the Plum Creek System does not correlate to the amount of construction costs incurred by Monarch to serve Windy Hill. Additionally, B&D reduced the private easement cost of $20,000 per acre proposed by Monarch by 50% to $10,000 per acre.[13] But for this decertification, Monarch would not have to incur any cost for this private easement. Therefore, Monarch should be fully compensated for the entire cost associated with this additional easement that will now be required to provide service to its customers.

As a result of these two errors by the third appraiser, the amount for this factor was reduced by nearly half a million dollars to $221,702.[14] Monarch should be compensated for the full impairment of service and increased cost to existing customers of $708,800. Denial of this compensation amounts to a penalty on Monarch's existing customers who will be forced to bear the burden of these additional costs.

Factor 8 - Other Relevant Factors: $2,266,600

Monarch seeks $2,266,600 associated with the market value of the Windy Hill Tract, based on the future returns to investors from water sales. However, B&D concluded that a current value could not be calculated for any future returns to investors because neither a future

---

[11] JHA Report at 5 (July 19. 2013).

[12] B&D Report at 5 (Aug. 14, 2013).

[13] *Id.*

[14] B&D Report at 5 (Aug. 14, 2013).

rate base nor a number of future connections is known at this time. In contrast, JHA concluded that to provide just and due compensation, a market value approach is appropriate to account for the value. Monarch is an investor owned utility and the denial of consideration of the market value will create additional risks for investor owned utilities as their risk of future investments being devalued increases. Therefore, JHA explained that the market value should be based on future returns, or profits, that are expected from water sales. The return on equity per equivalent meter was calculated by dividing the ROE plus income tax by the total equivalent connections. The NPV over the next 20 years was calculated using an 11.2% discount rate, which was the ROE submitted in Monarch's 2012 rate/tariff change application. The result was a market value of $2,266,600.[15]

III. CONCLUSION

WHEREFORE, PREMISES CONSIDERED, Monarch respectfully requests the TCEQ order that Monarch is due $3,748,489 for the property associated with the transfer of the CCN.

Respectfully submitted,

LLOYD, GOSSELINK,
ROCHELLE & TOWNSEND, P.C.
816 Congress Avenue, Suite 1900
Austin, Texas 78701
Telephone: (512) 322-5830
Facsimile: (512) 472-0532

LAMBETH TOWNSEND
State Bar No. 20167500

MELISSA A. LONG
State Bar No. 24063949

ATTORNEYS FOR MONARCH UTILITIES I, L.P.

---

[15] JHA Report at 6 (July 19, 2013).

CERTIFICATE OF SERVICE

I, Lambeth Townsend, hereby certify that on this 1st day of November, 2013, a true and correct copy of the foregoing document was transmitted as follows:

Lanny S. Lambert, City Manager
City of Kyle
100 West Center St.
Kyle, Texas 78640
Telephone: (512) 262-3927
Facsimile: (512) 262-3987

Docket Clerk
TCEQ Office of Chief Clerk MC 105
P. O. Box 13087
Austin, Texas 78711-3087
Telephone: (512) 239-3300
Facsimile: (512) 239-3311

Ronald J. Freeman
Freeman & Corbett
8500 Bluffstone Cove, Suite B-104
Austin, Texas 78759
Telphone: (512) 451-6689
Facsimile: (512) 453-0865

Brian Christian
TCEQ SBEA Division
Public Participation and Education Program MC 108
P. O. Box 13087
Austin, Texas 78711-3087
Telephone: (512) 239-4000
Facsimile: (512) 239-5678

Bret Fenner, P.E.
B & D Environmental, Inc.
P. O. Box 500264
Austin, Texas 78750
Telephone: (512) 264-9124
Facsimile: (512) 692-1967

Brian Dickey Elizabeth Flores
TCEQ Water Supply Division MC 159
P. O. Box 13087
Austin, Texas 78711-3087
Telephone: (512) 239-4691
Facsimile: (512) 239-2214

Hollis Henley
TCEQ Litigation Division MC 175
P. O Box 13087
Austin, Texas 78711-3087
Telephone: (512) 239-0600
Facsimile: (512) 239-3434

Blas Coy
TCEQ Office of Public Interest Counsel MC 103
P. O. Box 13087
Austin, Texas 78711-3087
Telephone: (512) 239-6363
Facsimile: (512) 239-6377

LAMBETH TOWNSEND

3176/09/4246748